Salt Sustainable Global Shares Fund Fact Sheet – January 2024

Manager Profile

Salt Funds Management is a boutique investment management firm wholly owned by its employees which specialises in actively seeking to maximise returns while managing the risks of the investment. Salt examines investments for their environmental and social impact as well as the quality of their governance.

Investment Strategy

The Fund's investment objective is to outperform (after fees and expenses but before tax) the MSCI World (Net) Index in New Zealand dollars on a rolling three-year basis. To achieve this, the Fund targets a portfolio of global companies with high total return potential and high Environmental, Social and Governance (ESG) factor scores.

The strategy seeks to provide attractive long-term returns with less long-term volatility than the broader market by reducing the risks associated with poor ESG outcomes. The Fund will seek to achieve its investment objective by investing primarily in global equity.

Fund Facts at 31 January 2024

Benchmark	MSCI World (Net) Index in NZD
Fund Assets	$63.64 million
Inception Date	12 July 2021
Underlying Manager	Morgan Stanley Investment Management

Unit Price at 31 January 2024

Application	1.1957
Redemption	1.1908

Investment Guidelines

The guidelines for the Sustainable Global Shares Fund are:

Global Equities	95% – 100%
Cash	0% – 5%

Target investment Mix

The target investment mix for the Salt Sustainable Global Shares Fund is:

Global equities	100%

Fund Allocation at 31 January 2024

Global equities	98.5%
Cash	1.5%

Fund Performance to 31 January 2024

Period	Fund Return*	Benchmark Return
1 month	5.08%	4.09%
3 months	10.36%	9.72%
6 months	8.12%	6.47%
1 year	23.62%	22.82%
2 year p.a.	6.66%	7.47%
Since inception p.a.	8.51%	8.70%
5 year p.a.*	14.97%	14.08%

Performance is before fees and tax and adjusted for imputation credits. Benchmark performance is gross. Past performance is not a guarantee of future results. Data as of 31 January 2024. *5 year strategy performance is also gross of fees.

Fund ESG Scores	Portfolio	Index
Sustainable Global Shares	26T CO2 /$m	162T CO2 /$m
Portfolio Carbon Footprint:	15% of MSCI World Index*	

Source: MISM Quarterly Investment Report & Trucost based on the Scope 1 & 2 carbon emissions per $1million of Portfolio companies' sales, and as weighted average carbon intensity (WACI). *As at 31 January 2024, the Portfolio's carbon footprint was 85% lower than the MSCI World Index and 84% below AC World.

Top 10 holdings	
Microsoft (US)	Constellation Software (CA)
SAP (DE)	Thermo Fisher Scientific (US)
VISA (US)	RELX (UK)
Accenture (US)	Becton Dickinson (US)
Intercontinental Exchange (US)	Reckitt Benckiser (UK)

Source: MSIM, data as at 31 January 2024.
The Top 10 Holdings represented 42.66% of the total portfolio.

Market Review

- After a strong December month, markets were more circumspect in the New Year. Strong activity data, particularly in the US, was received favourably by equity markets, but that came with push-back from central banks of early expectations of rate cuts, which wasn't viewed favourably by fixed income markets. Developed market equities rose 1.2% (in USD) over the month while the global aggregate bond index was down by -1.4% (also in USD).
- This moderate gain was however boosted in unhedged NZ dollar terms by the weakening in the NZD during January. NZD/USD declined -3.2%.
- In the US, data was more in line with a "no landing" than a "soft landing" scenario. The first estimate of December 2023 GDP data was exceptionally strong (+3.3%, q/q annualised), as was the December labour market report (unemployment rate unchanged at 3.7%). The euphoria was tempered somewhat later in the month by a hawkish tone to the Fed's January statement and by Fed officials' comments.

- The European Central Bank left interest rates unchanged in January and reiterated they would remain data dependent. That was followed by the composite purchasing managers index (PMI) rising to 47.9 in January. That's its highest level in three months, but still well below the benchmark 50 that separates expansion from contraction.
- In Japan, the TOPIX was the best performing major equity market over the month. This was helped by the Bank of Japan leaving monetary policy unchanged amid speculation (including ours) that we would soon see an end to their Negative Interest Rate Policy (NIRP) and Yield Curve Control (YCC). That now appears more likely in April.
- In China, December 2023 quarter GDP growth came in at 5.2% y/y, broadly in line with expectations but soft relative to history. Partial activity data also remained weak. The PBoC continued to add stimulus over the month, but this remains largely reactive and somewhat timid. We expect a fiscal package to support consumption in the next few months.
- In Australia, December 2023 quarter inflation came in below expectations at both the headline and core (trimmed mean) level. This followed weaker-than-expected retail sales and employment data. This combination of news means the RBA is more-than-likely done with interest rate hikes and will adopt a neutral bias at its February meeting.
- In New Zealand, December 2023 quarter inflation data also came in below expectations, but in a somewhat unbalanced fashion. All the downside surprise came in tradeable goods (imported inflation), while non-tradeable (domestic inflation) came in stronger than expected. This prompted a warning to markets from the RBNZ's Chief Economist, that while progress was being made in the disinflation journey, there was still a long way to go, effectively pushing back on early rate cut expectations. We don't expect a first OCR cut until November.

Portfolio Review

- In January month, the Portfolio returned +5.08% (NZD/Gross), ahead of the MSCI World Net Index which returned +4.09%. The Portfolio delivered strong absolute performance for the one-year period, returning +23.62%, which lifted its 12-month return 80bps above the index's +22.82% performance for the period.
- Given the Portfolio is designed for long-term capital appreciation through compounding and reduced downside participation, lagging the index in such a sharp up-year as 2023 can occur, as it previously did during the second half of 2020. This resolved in January 2024.
- The January outperformance was due to sector allocation as the underweight in Consumer Discretionary, the zero weight in Materials and the overweight in Information Technology helped performance. Stock selection was negative as weakness in Health Care and Financials more than offset strength in Information Technology and Consumer Staples.
- The largest contributors to absolute performance during the month were SAP (+85 basis points [bps]), Microsoft (+56 bps), Constellation Software (+48 bps), VISA (+41 bps) and Accenture (+35 bps).
- The largest absolute detractors were IQVIA (-25 bps), AIA (-20 bps), Texas Instruments (-6 bps), Atlas Copco (-6 bps) and ADP (-19 bps) and Nike (-2 bps).

Commentary & Outlook (Morgan Stanley Investment Management)

After a boisterous end to 2023, the MSCI World Index was significantly more muted in January, returning +1.2% in U.S. dollars (USD) and +1.8% in local currency (+4.1% in NZD). Exposure to continued AI optimism saw Communication Services and Information Technology (both +4%) finish as the month's top performers, helped by Netflix (+15%) and Meta (+10%) and Nvidia (+24%) and ASML (+15%) respectively.

Health Care (+3%) also outperformed the MSCI World Index, while Financials and Consumer Staples (both +1%) were in line. All other sectors finished in the red with the lower quality, more cyclical sectors – notably Real Estate (-4%) and Materials (-5%) – finishing at the bottom.

Turning to geographies, the U.S. (+2%) was only a touch ahead of the index in the month. Japan (+5% USD, +8% local currency) was the only other major market to outperform in USD and local currency, well ahead of its Asian peers Singapore (-4%, -3%) and Hong Kong (-10%, -10%).
Looking at the major European markets as a whole: Italy, France and Switzerland (each 0%, +2%) marginally outperformed in local currency but lagged in USD, while Germany (-1%, +1%), Spain (-1%, +0%) and the UK (-1%, -1%) were all slightly behind the index.

Driving Quality

As a team, we've spent the last quarter of a century seeking out what we consider to be the world's best compounders. These are companies we believe can continue to steadily – and organically – grow their earnings and free cash flows at an attractive rate for the long term.

Compounding is a powerful force. Grow $1,000 at 10% over seven years and you will have doubled your money. Continue for another 10 years and you'll have $6,000.

We have two principal tasks. One is finding compounders. The second is striving not to overpay. If a company is too expensive then it is too expensive – and you run the risk of the price receding to a fair and sensible level. The recently departed Charlie Munger famously said, "A great business at a fair price is superior to a fair business at a great price." We agree. In his inimitable style, Munger also said, "If you buy something because it is undervalued, then you have to think about selling it when it approaches your calculation of intrinsic value. That's hard. But, if you can buy a few great companies, then you can sit on your ****.... That's a good thing." Here, we are less inclined to agree. The truth is, you can't just sit and watch – it is essential to check and check again the compounding potential is intact and not under threat, that there's no risk of fading returns, and that the valuation remains reasonable. That's a challenge we meet with rigorous fundamental analysis and company engagement.

Driving Quality…continued

What tells us a company might be a high-quality compounder? We have two measures that are part of our quantitative screen, the principle one being Return on Operating Capital Employed, or ROOCE, and the other being gross margin. ROOCE isn't a measure readily found in FactSet or Bloomberg screening tools; even if you Google it, the search will likely default to ROIC (Return on Invested Capital). ROOCE isn't an invention of ours, however.

It is a subset of ROIC (also an important measure; it includes goodwill and accounts for past capital allocation decisions). Essentially, what ROOCE tells us is how much incremental capital is required to grow a business. Using a car analogy, if we think of ROIC as the quality of the car engine and the driver's historical capability, ROOCE is only the quality of the car engine.

Historically, our analysis shows that high ROOCE companies have had a better annualised long-term return than low ROOCE companies. Using 20 years of data for the MSCI World Index and dividing the constituents into five buckets, split highest to lowest by ROOCE, the highest ROOCE bucket returns 10.5% annualised, the next returns 10.2%, then 9.5%, then 8.5% and finally 7.5% for the lowest bucket.1 At first glance the spread might not seem that wide. But if we think of it in terms of compounding, $1,000 for 10 years at 10.5% rather than 7.5% results in $2,456 instead of $1,917 – nearly 30% more. Compounding matters.